

Chapter Six

Fund Costs

Introduction

6.1 This chapter examines the impact of the portability regulations on fund costs, with specific reference to:

- a) Multiple roll over/transfer costs;
- b) Partial roll over/transfer costs; and
- c) Revised benefit designs.

Multiple roll over/transfer costs

6.2 As indicated in Chapter One, regulation 6.33 of the draft Superannuation Industry (Supervision) Amendment Regulations 2003 allowed unlimited roll overs/transfers out of a superannuation account.

6.3 A large number of parties making submissions to the inquiry opposed this provision on the basis of its cost impact on funds. For example, the Law Council of Australia argued that the draft regulations would create an unnecessary administrative burden, and could result in members treating a superannuation interest like a bank account.¹

6.4 In turn, ASFA argued that the introduction of portability without choice would create a new class of exiting member (a partial active-account exit), which would require funds to establish new processing arrangements with associated additional costs. ASFA noted that rather than just closing an account, funds would be required to make the roll over/transfer, update the member record to reflect the individual benefit component rolled over/transferred, record this as a regulation 6.33 request and so on.²

6.5 Similar concerns regarding higher fund costs were also raised by Mercer,³ the AIG⁴ and the Corporate Super Association.⁵

1 *Submission 20*, Law Council of Australia, p. 3.

2 *Submission 2*, ASFA, p. 4.

3 *Submission 17*, Mercer, p. 3.

4 *Submission 5*, AIG, p. 2.

6.6 Given such concerns about the costs of portability, many parties to the inquiry further argued for limits to be placed on the number of roll overs/transfers available to fund members:

- IAA recommended that the Government assist funds to control costs by allowing trustees to limit the numbers of roll over/transfer requests from any member to no more than say, one a year.⁶
- MTAA Super advocated that any portability arrangements should require a minimum period (say 12 months) before a second and subsequent full or partial roll over/transfer of an account balance could be requested.⁷
- CPA Australia advocated that consideration be given to limiting the timing of when portability can be exercised, such as on resignation from an employer or no more than once a year.
- The FPA recommended that a member have a limit of, say, two roll overs/transfers per year, to overcome some of the cost burden on funds.⁸

6.7 As indicated in Chapter One, the Government moved in the gazetted regulations to require trustees only to affect one roll over/transfer per year for each member of a fund, although they will be free to offer more regular roll overs/transfers if they wish. The Committee notes that in the hearing on 1 August 2003, Mr Ward from Mercer⁹ and Mr Shallue from IAA¹⁰ welcomed the restriction on roll overs/transfers to one a year.

6.8 Nevertheless, some concerns about the impact of the portability regulations on fund costs remained. For example, Mr Silk from IFF observed in the hearing on 1 August 2003:

In relation to the first issue—that is, a limit on the number of transfers to one per year—we submit that that is a significant improvement on the proposals contained in the original regulations. However, that is an improvement from a very low base. The original proposal—and we need not now go into the details—was fundamentally flawed and would have caused significant long-term damage to the retirement incomes of a number of Australians. It would have imposed significant additional cost pressures on the system as a whole that would have ultimately been borne by the members of superannuation funds.¹¹

5 *Submission 9*, Corporate Super Association, p. 5.

6 *Submission 15*, IAA, p. 3.

7 *Submission 6*, MTAA Super, p. 3.

8 *Submission 24*, FPA, p. 1.

9 *Committee Hansard*, 1 August 2003, p. 27.

10 *Committee Hansard*, 1 August 2003, p. 40.

11 *Committee Hansard*, 1 August 2003, p. 3.

6.9 Ms Galbraith from Superpartners also indicated that the restriction to one roll over/transfer in a year was a welcome change. However, she raised the following concern:

If we have the scenario of members who are receiving ongoing contributions taking their entire account balance every 12 months, we will have to close that member's account and then when the next contribution comes in create a new account for them in the same fund. This causes a number of administration issues for us, the most pertinent being that it is difficult to carry the member's history across.¹²

6.10 In response to such arguments for restrictions on transfers, however, Mercer submitted that there is an argument for placing no restriction on the number of roll overs/transfers if portability is to work effectively for members, assuming the members paying an appropriate exit fee each time.¹³

6.11 APRA also acknowledged that members may seek regular roll overs/transfers out of a fund and that this would raise administration costs. Accordingly, APRA noted that trustees will need to ensure that administration systems (including those of service providers) are such that information (including on current member benefits and exit fees) can be given on request to prospective transferors, that inward and outward transfers can be effected and that disclosure requirements (including in relation to possible changes to insurance cover) are met.¹⁴

Partial roll over/transfer costs

6.12 Similar to concerns raised above about the impact of frequent fund roll overs/transfers on fund costs, a number of parties to the inquiry also highlighted the impact of partial roll overs/transfers on fund costs.

6.13 For example, Watson Wyatt argued that allowing partial roll overs/transfers of withdrawal benefits at any time will increase fund costs through additional benefit processing, investment costs and surcharge reporting. Accordingly, Watson Wyatt argued that the draft regulations should make it clear that the additional costs incurred from portability are able to be allocated equitably between those members who request a fund roll over/transfer.¹⁵

6.14 Similar concerns were expressed in hearings. For example, Mr Watson from MTAA Super indicated in the hearing on 31 July 2003:

12 *Committee Hansard*, 1 August 2003, p. 13.

13 *Submission 17*, Mercer, p. 3.

14 *Submission 14*, APRA, p. 4.

15 *Submission 12*, Watson Wyatt, p. 2.

Our view is that partial rollovers will actually create the opposite effect to what the regulations are seeking to do in terms of reducing the costs, increasing competition and improving the lot of members.¹⁶

6.15 Similarly, Dr Anderson from ASFA indicated in the hearing on 31 July 2003 her opposition to partial roll overs/transfers.¹⁷

6.16 Given these concerns, the Committee notes that a number of parties to the inquiry also recommended that partial roll overs/transfers be restricted or prohibited:

- AIST recommended that members be restricted to one partial roll over/transfer per year.¹⁸
- The Law Council of Australia suggested that the draft regulations ought to either prescribe the number of times annually a member can make a request for a partial roll over/transfer or give the trustee the power to determine how frequently a request can be made.¹⁹
- IAA recommended that trustees be given discretion to refuse requests for partial roll overs/transfers.²⁰
- The CPA Australia advocated that individuals only be allowed to roll over/transfer the whole of their superannuation benefits, in the interests of maintaining a simple system and ensuring that the administrative burden on superannuation providers is minimised.²¹

6.17 Similar positions were also expressed in hearings. Ms Ryan from AIST indicated in the hearing on 31 July that short of the regulations being deferred to coincide with the introduction of choice, AIST would like roll overs/transfers, including partial roll overs/transfers, to be restricted to one a year.²² Mr Shallue from IAA argued that trustees should be given further discretion to refuse requests for partial roll overs/transfers.²³

6.18 Once again, the Committee notes that Government partially addressed this matter in the gazetted regulations by limiting the number of roll overs/transfers, including partial roll overs/ transfers, to one a year.

16 *Committee Hansard*, 31 July 2003, p. 12.

17 *Committee Hansard*, 31 July 2003, p. 17.

18 *Submission 11*, AIST, pp. 2-3.

19 *Submission 20*, Law Council of Australia, p. 3.

20 *Submission 15*, IAA, p. 3.

21 *Submission 13*, CPA, p. 2.

22 *Committee Hansard*, 31 July 2003, p. 25.

23 *Committee Hansard*, 1 August 2003, p. 40.

Revised benefit design

6.19 In its written submission, Mercer argued that there are many funds which will need to change their benefit design in order to properly cater for portability. This will require advice to members and changes to trust deeds, product disclosure statements, other communication material, administration systems and so on. Mercer cited two examples:

- a) One example is an accumulation fund where the death benefit is the greater of 5 times salary and the member's account balance. If the member elects to roll over/transfer part or all of the account balance, this would result in a higher level of insurance being required to maintain the pre-roll over/transfer benefit. It may therefore be appropriate (or necessary) for the benefit of 5 times salary to be similarly reduced. (If not reduced, then the higher level of insurance would have to be funded by the member, the employer or other members.)
- b) A second example is a partially vested accumulation fund. In such a fund it would not be possible to merely reduce the partially vested account by the amount rolled over/transferred. Significantly more complex procedures would be involved.

6.20 Mercer submitted that changes in benefit designs will result in additional costs to funds from changing the governing rules, changing the administration systems, changing communication material and a more complex benefit design. Accordingly, Mercer argued that funds will need to be given at least 12 months to put appropriate systems in place.²⁴

24 *Submission 17, Mercer, p. 4.*